

GENERAL OBLIGATION DEBT SERVICE SUMMARY

The City of Houston's General Debt Service Fund (the "Fund") accumulates resources for the principal and interest payments on tax supported debt consisting of: general obligation bonds/refunding bonds, claims and judgment bonds, annexed districts' bonds, pension bonds, certificates of obligation, and general obligation commercial paper notes (the "Obligations"). Payments for arbitrage rebate and administrative fees to administer the debt program (paying agent, lines of credit, rating agencies and other professional services) are also accounted for in the Fund. The debt service requirements for FY2011 are estimated to be \$310 million.

The largest revenue source for the Fund is the General Fund, which transfers a portion of ad valorem taxes (property tax receipts) required for debt service on the Obligations. Within the limits prescribed by law, the City is obligated to assess, levy, and collect annual ad valorem taxes sufficient to pay the principal of, and interest, on the Obligations. The Constitution of the State of Texas limits the maximum ad valorem tax rate to \$2.50 per \$100 assessed valuation for home-rule cities such as the City of Houston (the "City"). In addition, Proposition 1 limits increases in the City's ad valorem tax revenues by requiring voter approval for increases in ad valorem taxes in future years above a limit equal to the lesser of the actual revenues in the proceeding fiscal year, plus 4.5%, or a formula that is based upon the actual revenues received in Fiscal Year 2005 adjusted for the cumulative combined rate of inflation and the City's population growth plus credits for previous years that fall under the cap. The City's tax rate for Fiscal Year 2010 (Tax Year 2009) was \$0.63875 (per \$100 assessed valuation), which consists of \$0.457284 for general purposes and \$0.181466 for debt service. The proposed Fiscal Year 2011 Budget includes a tax rate of \$0.63875 (per \$100 assessed valuation) for Fiscal Year 2011 (Tax Year 2010).

The City's current policy states that the annual contribution from the General Fund for general obligation debt service should not exceed 20% of the total General Fund revenues, excluding state and federal grants. The budgeted FY2011 General Fund transfer to pay debt service is approximately 13.54% of expected General Fund revenues.

The second largest source of revenue for the Fund is third party reimbursements. Third party reimbursements are from various parties that have special agreements with the City. Entities that have entered into these agreements with the City include but are not limited to the Metro Transit Authority of Harris County, Buffalo Bayou Partnership, Texas Medical Center and Federal Emergency Management Agency (FEMA). The City uses various commercial paper programs to initially fund certain projects but receives reimbursements to retire the appropriate portion of the commercial paper.

Another source of revenue for the Fund are annual charges to the Combined Utility System Fund to compensate the Debt Service Fund for the cost of paying debt service on certain tax bonds and assumed bonds. The sewer portion of the Combined Utility System is also charged for debt service payments on certain tax bonds issued for sewer purposes.

Other sources include but are not limited to debt service reimbursement for special financings that vary from year to year. Examples of special financings include the Lake Houston Tax Increment Reinvestment Zone (Lake Houston TIRZ) and lighting retrofit projects being implemented by the General Services Department (GSD). Interest earned on construction funds (as a result of bonds issued) may be used as a revenue source to help fund debt service and may also be used for expenditures incurred for administering bond programs.

The FY2011 Annual Financing Plan is presented to outline the anticipated sale of City bonds, Certificates of Obligation, pension bonds, tax and revenue anticipation notes and commercial paper notes for the upcoming fiscal year. It is expected that the City will issue a total ranging from \$0.85 to \$1.50 billion, depending on needs and market conditions.

The Obligations are issued in both fixed and variable rate structures. The City's current policy is to maintain approximately 20% of the Obligations in a variable rate structure. The City currently issues variable rate commercial paper notes to initially fund various projects. When the amount of outstanding commercial paper notes reaches a level of 20% of total outstanding debt, or is otherwise deemed prudent, the commercial paper notes are refunded with fixed rate bonds to lock in a portion of the outstanding commercial paper notes at a fixed rate to minimize interest rate exposure.

Tax Bonds and Certificates of Obligation

The Obligations issued as fixed rate debt bear yields ranging from 0.20% up to 6.29%, which are established at the time of issuance and are based on market rates. The City's policy is to keep the combined weighted average life of the fixed rate debt at or below 12 years. The City issues Tax Bonds to provide for permanent financing through refinancing of commercial paper notes or refunding previously issued and outstanding Tax Obligations of the City. The City has issued Pension Obligation Bonds in FY2005 - FY2010 and is expected to issue more in FY2011. Pension Obligations Bonds are payable from and secured by ad valorem taxes and/or revenues to fund unfunded actuarial accrued liabilities ("UAAL") associated with its pension funds.

The City may also issue Certificates of Obligation payable from ad valorem taxes and, in some cases, a pledge of certain City revenues for the purpose of paying any contractual obligations. Certificates of Obligation are issued for special financings and demolitions of dangerous buildings.

The budget includes a seven-month reserve for Tax Bonds and Certificates of Obligation. This reserve covers principal and interest payable in the first seven months of the following fiscal year.

Variable Rate Debt -Commercial Paper Notes

The General Obligation Commercial Paper Program, Series D ("Series D") has total available authorization of \$212 million and General Obligation Commercial Paper Program, Series G ("Series G") has total available authorization in the amount of \$276 million. Series D and Series G provides for the issuance of voter-authorized obligations related to the 2001 and 2006 bond elections and both series have been implemented to fund various public improvement projects in the Capital Improvement Plan (the "CIP").

The City authorized General Obligation Commercial Paper Program, Series E ("Series E") with a total available authorization of \$325 million, under Chapter 1431, Texas Government Code, as amended (voter authorization not required). The City authorized General Obligation Commercial Paper Program, Series F ("Series F") with a total available authorization of \$101 million under Chapter 1431, Texas Government Code, as amended (voter authorization not required) to fund certain capital improvements related to drainage.

The City authorized General Obligation Commercial Paper Program, Series H ("Series H") with a total capacity of \$200 million. The Series H Notes is a supplement to the Series D, Series G, and Series F Notes but is not an increase of total authorization.

The commercial paper programs serve as a management tool to access the credit market to meet cash needs while minimizing the rebate liability on unspent proceeds. The commercial paper notes are refunded periodically to fixed rate tax bonds to limit the City's variable rate exposure and to match the average life of bonds to the life of the assets purchased. Interest on the notes varies depending on the market conditions. The notes may be issued for a period not to exceed 270 days and will bear interest based upon the specified terms, but initially not to exceed 6.5%. The reserves for the notes are based on the amount projected to be outstanding during the fiscal year. For FY2010, average all-in interest cost for variable rate obligations was approximately 1.0%. The budgeted all-in interest cost for the City's variable rate obligations in FY2011 is 2.5%. The budget includes reserves for interest on commercial paper notes to provide for fluctuations in interest rates at a rate of 6.0% of the estimated amount to be outstanding during the fiscal year.

Assumed Bonds

Prior to FY1991, the City had an aggressive annexation program. However, no annexations took place during FY1991 and FY1992 until the period from FY1993 to FY1997 during which the City completed seven new annexations. Although annexations have benefited the City in economic growth, no additional annexations have occurred since FY1997. Since FY1999 the legislation requires the City to adopt a three-year annexation plan, and with certain exceptions, only those areas identified in such plan would be eligible for annexation. The City does not currently have a plan in place to annex additional districts. Debt assumed by the City from annexations of various districts within the extra-territorial jurisdiction becomes a part of the City's debt service requirements. During FY2007 all the debt related to annexation has been refunded.

Interest Rate Swaps

As part of its debt management program, the City considers and reviews various interest rate swap proposals, including tax supported interest rate swaps, consistent with the guidelines set forth in its Interest Rate Swap Policy adopted on November 25, 2003. On February 20, 2004, with respect to certain outstanding Tax Bonds, the City entered into a tax supported interest rate swap agreement with Rice Financial Products Corp. LLC (RFP). Under this Swap Agreement, the counter party (RFP) effectively paid a variable interest rate based on the London Interbank Offered Rate ("LIBOR") plus a fixed spread, and the City paid a variable interest rate, based on a Securities Industry and Financial Markets Association ("SIFMA," formerly Bond Market Association "BMA") tax exempt rate, times a notional principal amount equal to \$200 million. The underlying bonds were Public Improvement Bonds (PIB) issued between 1998 and 2005 with various maturities. The initial payment date was March 1, 2005, and thereafter payments continued every September 1 and March 1 through 2009. This swap was terminated at the City's option on August 25, 2009. An accumulated profit of approximately \$8 million was earned on this swap.

Drainage Supplemental Debt Service Fund

In FY2009 City Council instituted the Drainage Supplemental Debt Service Fund for the purpose of funding additional long-term drainage initiatives. The program calls for an annual set aside of a pre-determined portion of ad valorem tax receipts, as approved by Council annually. The proposed set-aside amount is equal to \$0.0040 per \$100 of ad valorem tax valuation for FY2011.

Ad Valorem Tax Obligations of the City

State law permits the City to incur total bonded indebtedness through the issuance of voter authorized ad valorem tax bonds in an amount not to exceed 10% of the total appraised valuation of property in the City. The schedule below shows an estimate for the current fiscal year of outstanding debt applicable to the statutory limitation.

(in thousands of dollars)

Appraised Value (1)		<u>\$ 195,978,012,388</u>
Debt Limit, 10% of Appraised Value		\$ 19,597,801,239
Debt applicable to limitation (2)		
Public Improvement Bonds	\$2,319,930	
Commercial Paper Notes	247,533	
Pension Obligation	587,525	
Certificates of Obligation	<u>70,160</u>	
Total Debt Applicable to Limitation	\$3,225,148	
Less:		
Amount available for repayment of general obligation debt (2)	<u>(181,326)</u>	
Total debt applicable to limitation		<u>\$ 3,043,822</u>

(1) Appraised value for the Fiscal Year 2010 (Tax Year 2009), as of February 26, 2010.

(2) Estimated balance for fiscal year ending June 30, 2010.

Outstanding General Obligation Debt

(in thousands of dollars)

	FY2008	FY2009	FY2010	FY2011
	Actual	Actual	Estimate	Budget
OUTSTANDING DEBT:				
Public Improvement Bonds	\$1,798,150	\$1,988,300	\$2,319,930	\$2,182,775
Commercial Paper Notes	\$ 625,950	\$ 519,200	\$ 247,533	\$ 323,335
Pension Obligation	\$ 567,481	\$ 585,525	\$ 587,525	\$ 607,525
Certificates of Obligation	\$ 88,875	\$ 82,832	\$ 70,160	\$ 71,095
Annexed Districts' Bonds	\$ -	\$ -	\$ -	\$ -
TOTAL OUTSTANDING DEBT	\$3,080,456	\$3,175,857	\$3,225,148	\$3,184,730

The strength of the City's general obligation debt is reflected in the statements of the ratings agencies:

Standard & Poor's (AA) - "The stable outlook reflects the City's "sizable and diverse economic base, which has shown marked resiliency over the past year; positive financial operations with a strong general fund reserve balance, although the balance is anticipated to decline; and management's continued commitment to control expenditure growth and address the City's contingent liabilities."

Moody's (Aa2) - "The rating reflects the City's large tax base that is expected to experience a significant moderation of growth in the medium term, favorable financial position and manageable debt burden. The positive outlook reflects Moody's expectation that despite current economic conditions that are impacting key revenue sources, the City will maintain a satisfactory financial position through strong budget management."

Fitch - "The 'AA' ratings denote expectations of very low default risk. They indicate very strong capacity for payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events."

Principal and Interest Payable from Ad Valorem Taxes

Existing debt as of April 13, 2010

Fiscal Year	Tax Bonds		Pension Obligations	
	Principal	Interest	Principal	Interest
2011	137,155,000	116,912,762	0	35,416,883
2012	130,620,000	110,071,474	0	35,416,883
2013	125,615,000	103,584,612	0	35,416,883
2014	131,285,000	97,211,618	6,345,000	35,416,883
2015	141,665,000	90,731,355	6,790,000	35,017,782
2016	145,740,000	83,589,274	7,265,000	34,590,691
2017	157,410,000	76,330,637	7,770,000	34,133,723
2018	160,920,000	68,548,687	8,315,000	33,644,990
2019	138,010,000	60,440,375	8,895,000	33,121,976
2020	154,140,000	53,721,550	9,520,000	32,562,481
2021	128,395,000	46,080,675	20,145,000	31,963,673
2022	122,725,000	39,627,563	21,440,000	30,696,552
2023	134,815,000	33,459,463	22,805,000	29,347,976
2024	84,765,000	26,718,713	24,265,000	27,913,542
2025	88,140,000	22,475,138	25,820,000	26,387,273
2026	54,345,000	17,982,238	27,475,000	24,763,195
2027	73,820,000	15,264,988	29,235,000	23,035,018
2028	75,925,000	11,502,288	31,100,000	21,196,136
2029	43,345,000	7,257,408	41,425,000	19,239,946
2030	8,285,000	4,697,845	43,995,000	16,716,046
2031	8,715,000	4,276,676	58,135,000	14,034,804
2032	11,610,000	3,837,770	61,650,000	10,558,028
2033	12,190,000	3,257,651	22,965,000	6,869,887
2034	10,080,000	2,648,482	0	5,625,280
2035	13,310,000	2,143,401	44,345,000	5,625,280
2036	11,120,000	1,473,320	35,400,000	3,198,102
2037	8,265,000	895,537	22,425,000	1,241,897
2038	5,115,000	444,890	0	0
2039	2,405,000	150,024	0	0
	2,319,930,000	1,105,336,414	587,525,000	643,151,807

FISCAL YEAR 2011 BUDGET

Tax Certificates		Total
Principal	Interest	Debt Service
3,250,000	3,398,880	296,133,524
6,250,000	3,268,870	285,627,227
11,095,000	2,984,380	278,695,874
2,890,000	2,458,085	275,606,586
3,010,000	2,341,805	279,555,943
3,155,000	2,196,985	276,536,950
3,310,000	2,044,415	280,998,774
3,470,000	1,883,565	276,782,241
3,640,000	1,714,115	245,821,467
3,820,000	1,535,495	255,299,526
4,005,000	1,347,150	231,936,498
4,205,000	1,148,750	219,842,865
3,395,000	938,500	224,760,939
3,565,000	768,750	167,996,005
3,745,000	590,500	167,157,911
3,935,000	403,250	128,903,683
4,130,000	206,500	145,691,506
0	0	139,723,424
0	0	111,267,354
0	0	73,693,891
0	0	85,161,480
0	0	87,655,798
0	0	45,282,538
0	0	18,353,762
0	0	65,423,681
0	0	51,191,422
0	0	32,827,434
0	0	5,559,890
0	0	2,555,024
70,870,000	29,229,995	4,756,043,216